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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

MARTIN L. STERN
DIRECT DIAL: (202) 662-8468

August 27, 1997

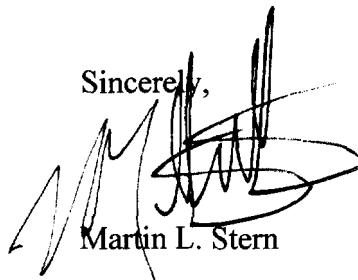
Mr. William Caton
Secretary
Federal Communications Commission
1919 M Street, N.W., Room 222
Washington, D.C. 20554

Re: Notice of Ex Parte Presentation, CC Docket No. 92-297, *et al.*

Dear Mr. Caton:

Pursuant to 47 C.F.R. § 1.1206(a)(2), WebCel Communications, Inc. ("WebCel") is filing with the Secretary an original and one copy of this notice of an ex parte presentation in the above-captioned proceeding. On August 27, 1997, David Mallof of WebCel, Frank Paganelli, of Blumenfeld & Cohen and I met with Peter Tenhula, of the Office of General Counsel. At this meeting, we discussed WebCel's view, as set out more fully in its Petition for Partial Reconsideration and its ex parte filings in this docket, that the LMDS designated entity rules should include a category for very small businesses and that the installment payment plan for LMDS designated entities should not be eliminated. WebCel also provided the attached handouts.

Sincerely,



Martin L. Stern

cc: Peter Tenhula, Esq.

Attachments

MLS/jkl

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July 21, 1997

Rosalind Allen, Esq.
Deputy Chief
Federal Communications Commission
Wireless Telecommunications Bureau
2025 M Street, N.W., Room 5002
Washington, D.C. 20554

Re: *CC Docket No. 92-297, et al. – Cook Inlet Proposal to Eliminate
Installment Payments*

Dear Ms. Allen:

We are writing in response to questions to WebCel Communications, Inc. ("WebCel") regarding its views on the proposal by Cook Inlet Region, Inc. ("Cook Inlet") to eliminate installment payments from the LMDS designated entity program.¹ These questions were posed by you, Kathleen O'Brian Ham, and Sande Taxali, as well as by Commissioner Ness, during recent *ex parte* meetings in connection with WebCel's petition for partial reconsideration of the LMDS *Second Report and Order*. This letter is also offered in light of televised remarks by Chairman Hundt last week forecasting the demise of installment payments as a designated entity preference for LMDS.

WebCel understands that this proposal stems from frustration at current attempts by certain PCS C Block auction winners to lobby the Commission to either forgive or restructure their debt obligations to the Government, and recognizes that the Commission may be becoming increasingly wary of future financing difficulties. *However, the complete elimination of installment payments for LMDS designated entities would be contrary to Congressional intent, well-established Commission policy to promote small business, and settled standards for agency policymaking, and must therefore be rejected.*

¹ See Petition for Reconsideration of Cook Inlet in CC Docket No. 92-297 at 5-6. During these meetings, we were also asked to provide additional support regarding WebCel's assertions as to the capital outlay required for the introduction of LMDS service, and, in particular, why LMDS is well-suited for small, start-up ventures. We have provided this information as part of WebCel's Reply, filed July 14, to Oppositions to its Petition for Reconsideration in CC Docket No. 92-297.

- ***The installment payment program for designated entities has been largely successful and is perhaps the Commission's key tool for promoting small business participation in spectrum-based services.***

In designing a system for competitive bidding, the Commission is required to "promot[e] economic opportunity and competition . . . by disseminating licenses among a wide variety of applicants, including small businesses" and to ensure that "small businesses . . . are given the opportunity to participate in the provision of spectrum-based services."² As the Commission has repeatedly found, *access* to capital, rather than just the *cost* of capital, is the most significant hurdle to entry by small businesses. The Commission has thus indicated that removing that barrier to entry for small businesses has been its "top priority" for spectrum policy.³

In order to promote the participation of small business and similar groups in spectrum-based services, Congress *required* that the Commission consider the use of installment plans in its arsenal of bidding preferences to assist small business and other designated entities.⁴ Previous successful auctions have proven that allowing installment payments for designated entities has achieved the objective for which they were established: to increase the participation of designated entities in spectrum auctions.⁵ In its recent *Competitive Bidding Order and Notice of Proposed Rulemaking*, the Commission again recognized the important role that installment payment plans have played in connection with small business access to capital and their participation in spectrum auctions.⁶

² 47 U.S.C. § 309(j)(3)(B), (4)(D).

³ See, e.g., *Report and Order*, Amendment of Parts 20 and 24 of the Commission's Rules-Broadband PCS Competitive Bidding and the Commercial Mobile Radio Services Spectrum Cap, 11 FCC Rcd 7824, 7846 (1996).

⁴ *Id.*, § 309(j)(4)(A), (D).

⁵ *Report*, Section 257 Proceeding to Identify and Eliminate Market Entry Barriers for Small Businesses, GN Docket No. 96-113, ¶ 43 (rel. May 8, 1997) ("*Market Barriers Report*") (noting that installment payments among measures taken by Commission to "enhance access to capital for small business in the auction process" and observing that "[u]pcoming auctions such as the LMDS auction also will offer small business installment payments").

⁶ *Order, Memorandum Opinion and Order and Notice of Proposed Rulemaking*, Amendment of Part 1 of the Commission's Rules – Competitive Bidding Proceeding, WT Docket No. 97-82, ¶ 34 (rel. Feb. 28, 1997) (installment payment plans, coupled with bidding credits "have resulted in new opportunities for small businesses to offer spectrum-based services" and are "useful tool for small business to access capital"); see also *Market Barriers Report*, ¶ 149 (tiered installment payment plans among the special incentives Commission continues to adopt "to encourage the participation of small businesses in auctions").

- ***Elimination of installment payments will resurrect substantial capital access barriers to small business participation in LMDS.***

Cook Inlet is unique among designated entities in that it has been granted exemptions from Commission affiliation rules (including for the LMDS auctions) under various statutory provisions and administrative determinations.⁷ These exceptions provide it with vast access to capital that would disqualify other entities from the small business designated entity category.⁸ This clearly distinguishes Cook Inlet from other designated entities eligible for bidding credits. For this reason Cook Inlet is hardly representative of typical small or very small business designated entities and its proposal cannot be viewed as such.

Most fundamentally, Cook Inlet's proposal ignores the importance of installment payment plans to small businesses *access* to capital, instead focusing on how *cost* of capital differences between large and small companies, even with the elimination of installment payments, may be remedied through larger bid discounts alone.⁹ While its proposal, if adopted, would not adversely affect its own interests, Cook Inlet's proposal would be devastating for typical designated entities, for whom *access* to capital, not just its *cost* (as the Commission has found over and over again), is the key barrier to participating in Commission auctions.

As Cook Inlet has pointed out, unlike commercial lending, the Commission's installment payment program is offered to all qualifying designated entities, with no pre-qualification by the Commission as to "credit-worthiness." Cook Inlet, however, has missed the essential point: the difficulty true small businesses face of being deemed "credit-worthy" by traditional commercial lenders *is exactly* the issue the installment program was designed to address. Unlike cost of capital issues, which are purely *quantitative*, access to capital issues for small businesses are derived in no small part from commercial lending practices, which are driven by *qualitative factors informed by subjective judgments*.

The reality is that commercial lenders may be unwilling to pre-commit funds to what is, in essence, a highly contingent endeavor created of necessity by the government, i.e., an auction. In the absence of an installment payment program, or some comparable form of guaranteed Government financing, a small business likely will have little or no ability to procure commercial debt financing prior to the auction for the balance due the U.S. Treasury, regardless of the level of discount. Therefore, small and very small businesses will be forced to participate in the auction with equity alone. In most instances, this capital structure will be insufficient, since nearly all of this equity would be paid to the government up-front, before buildout can occur, even though revenue, which can be used to repay the cost of the long-term asset, is generated

⁷ See *Order on Reconsideration* in CC Docket No. 92-297 ¶¶ 8-10 (rel. May 16, 1997).

⁸ *Id.*

⁹ Cook Inlet Petition at 10-11.

over a 10-year period. This is in stark contrast to larger bidders (including, presumably, Cook Inlet), who have existing lines of credit, can float commercial paper, or readily qualify for and obtain bridge funding.

In the absence of term payments, the capital access picture for small businesses would be further complicated by the Commission's designated entity control rules. Since lenders will not generally support debt financing for licensing, small businesses will be forced to also raise new, additional equity while being required to maintain compliance with the Commission's Rules on de facto and de jure control.

Overall, these very formidable access to capital hurdles faced by small and very small businesses have been thoroughly explored by the Commission throughout the history of the designated entity program. These barriers necessitated the implementation of the existing installment payments program and demonstrate the need for its continued existence.

- *Perceived problems in the C block auction do not justify the wholesale elimination of installment payments for LMDS designated entities.*

WebCel recognizes the probable catalyst for Cook Inlet's proposal—attempts by certain C block winners who overbid to lobby the Commission for forgiveness or restructuring of their debt obligations to the Government. Although the C block problems constitute today's frustration, we do not believe that legitimate concerns about the C block auction logically lead to the draconian policy conclusion that installment payment support for designated entities should be eliminated for future auctions, such as LMDS.

The Commission should neither lose heart nor its commitment to small and very small businesses based on its experience with the C block auction. Irresponsible and speculative bidding, unrealistic business cases, and a segregated designated entity auction design (which excluded larger bidders from the auction room), all coalesced in the C block auction. Given the increased attention of the money markets to bidding conduct and governance since the C block auction, the tightness of capital generally for spectrum auctions, and the fact that LMDS auctions will not be limited to designated entities, the potential for repeat of the C block experience seems remote, at best.

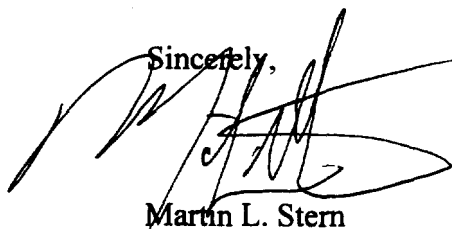
The Commission must not withdraw a *clearly effective policy initiative* in response to the first-time events of the C block auction. To do so would effectively exclude start-up firms and true entrepreneurs from the LMDS service, thereby "throwing out the baby with the bathwater." This would be contrary to the Congressional mandate underlying the Commission's competitive bidding authority and the Commission's own policy. Political expediency or administrative frustrations associated with the first-time events of the C block auction do not, in our view, provide the very substantial justification required by the Administrative Procedures Act and *Motor Vehicle Manufacturers Ass'n v. State Farm Mutual Ins. Co.*¹⁰ to support such a radical departure from the Commission's settled policy in this area.

CONCLUSION

WebCel believes that the Commission (with the addition of a very small business category as urged by WebCel in its Petition for Reconsideration) has already crafted appropriate and well-balanced rules, providing opportunities for success to designated entities, as well as measured and equitable penalties for misjudgment. Some form of an installment payment program is an important component of these rules for the continued success of the designated entity program.

Rather than adopt Cook Inlet's proposal, WebCel urges the Commission to enforce its existing rules in a clear, consistent and expeditious manner. At the same time, the Commission should maintain the common, established commercial practice, currently unavailable to true designated entities in the marketplace, of financing the acquisition of long-term assets via a government-supported term payment program. The simple action of holding steadfast to clearly articulated guidelines for those auction winners who irrationally bid, would greatly mitigate the possibility of over-exuberance of the part of future auction participants and, together with term payments, would continue to provide the opportunity for success to responsible designated entity participants.

Sincerely,



Martin L. Stern

Counsel for WebCel Communications, Inc.

cc: John Cimko, Kathleen O'Brien Ham, Nancy Boocker, Sande Taxali, Diane Conley, Mark Bollenger, Matthew Moses, Joe Levin, Linda Haller

Joe D. Edge, Mark F. Dever, *Counsel for Cook Inlet Region, Inc.*

Michael R. Gardner, *Counsel for CellularVision U.S.A., Inc.*

¹⁰ 463 U.S. 29 (1983).

WebCel Communications, Inc.

Recommendations for LMDS Auction

August 7, 1997

Ex parte presentation to FCC presented as follow-up to questions posed by the Commission staff during July 1997

Reinstate Very Small Business Categories for the LMDS Auction

1. Reinstate less than \$3 million average revenue category.
2. Reinstate between \$3 and \$15 million average revenue category.
3. Both categories receive a 35% bidding credit.
4. Interest rates and interest free periods for installment payments as specified in Docket 97-82.

Comments:

- * *Congruent with findings of February 1997 Order and NPRM in Docket 97-82. pg 23.*
- * *Very Small Business categories supported by the National Venture Capital Assn.*
- * *Order of magnitude between categories less critical than the overriding need for distinct differences between categories.*

Average gross revenues	Interest Rate	Payment Terms
Not to exceed \$3 million	T-note rate ⁶⁰	2 yrs. interest-only payments; amortize principal and interest over remaining license term
Not to exceed \$15 million	T-note rate + 1.5%	2 yrs. interest-only payments; amortize principal and interest over remaining license term
Not to exceed \$40-million	T-note rate + 2.5%	2 yrs. interest-only payments; amortize principal and interest over remaining license term
*Not to exceed \$75 million	T-note rate + 2.5%	amortize principal and interest over license term
*Not to exceed \$125 million	T-note rate + 3.5%	amortize principal and interest over license term

* These entities have never been defined as small businesses by our service-specific rules, but for broadband PCS they may have been eligible for installment payments as entrepreneurs.

The schedule set forth above is based in general on the plans adopted for our most recent auctions and, relying on our past auction experience, we believe these plans are appropriate. However, we recognize that plans with more generous terms were previously adopted for specific services.⁶¹ We seek comment on whether we should incorporate a schedule of

⁶⁰ The maturity date of the Treasury note would correspond with the license term for the particular service (e.g., a 10-year broadband PCS licensee would calculate its interest rate according to a 10-year T-note).

⁶¹ For instance, our broadband PCS rules confer on businesses with gross revenues of not more than \$75 million installment payment plans with an interest rate at the 10-year T-note rate plus 2.5 percent, with interest-only payments for the first year of the license. 47 C.F.R. § 24.716(b)(2). In comparison, the proposed plan for

Cost of Capital Differences Between Various-Sized Businesses (Based Upon Fair Market Value)

Marketable Majority Fair Market Value /1	Equity & Risk Free Rates /2	Equity Rate /1	Debt Rate	WACC / 3,4	Cost of Capital Advantage	
					Incremental	Cumulative
\$4,050,000	24.40%	19.38%	11.75%	15.73%		
\$6,750,000	23.60%	18.58%	10.75%	15.03%	0.70%	0.70%
\$13,500,000	22.40%	17.38%	10.25%	14.28%	0.75%	1.45%
\$67,500,000	19.80%	14.78%	9.75%	12.83%	1.45%	2.90%
\$135,000,000	18.70%	13.68%	8.75%	11.98%	0.85%	3.75%
\$1,350,000,000	14.90%	9.88%	7.85%	9.81%	2.17%	5.92%
\$13,500,000,000	11.10%	6.08%	7.35%	7.76%	2.05%	7.97%

Notes:

1. Abrams, Jay B. *Valuation. American Society of Appraisers. Volume 39, No. 2, pg. 14*
2. Assumes a risk free rate of 5% based upon the historical return on U.S Treasury bonds.
3. Weighted Average Cost of Capital.
4. Assumes a 1:1 debt to equity ratio.
5. Increases in interest rates effect smaller firms negatively disproportionate to this table.

Cook Inlet Proposal for LMDS DE Program without Installment Payments
Exacerbates Access to Capital Problem

	Very Small Business < \$15 Mil	Small Business \$15-40 Mil	Entrepreneur \$40-75 Mil
<u>Cook Inlet Proposal</u>			
Sample Bid	\$100	\$100	\$100
(Bidding Credit Percentage)	35%	25%	15%
Less: Bidding Credit	\$35	\$25	\$15
Net due immediately to U.S. Treasury	\$65	\$75	\$85

Effect of Cook Inlet Proposal on DEs

Downpayment @20% with Installment Program	\$13	\$15	\$17
Increase in Capital Raise Pre-Auction w/o Installment Program	\$52	\$60	\$68

Comments:

1. Very small businesses must raise, at minimum, 65 cents on the dollar upfront to responsibly participate in the auction.
2. Elimination of installment payments requires a minimum 4 times increase in upfront capital to participate.
3. Proposed level of bid discount is too low to compensate for the elimination of the installment payment program as currently structured.
4. Even if bid discounts were raised significantly - greater than 50% for very small business - the the access to capital problem is still left unsolved.

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WebCel Recommended LMDS DE Program With Installment Payments

	<u>Very Small Business</u>		<u>Small Bus</u>	<u>Entrepreneur</u>
	<u>< \$3 Mil</u>	<u>\$3-15 Mil</u>	<u>\$15-40 Mil</u>	<u>\$40-75 Mil</u>
Sample Bid	\$100	\$100	\$100	\$100
(Bidding Credit Percentage)	35.0%	35.0%	25.0%	15.0%
Less: Bidding Credit	\$35	\$35	\$25	\$15
Net Obligation to U.S. Treasury	\$65	\$65	\$75	\$85
(Required Downpayment Percentage)	26.0%	26.0%	23.0%	20.0%
Less: Immediate Downpayment to U.S. Treasury	\$17	\$17	\$17	\$17
Remaining Principal Financed By U.S.	\$48	\$48	\$58	\$68
Interest Rate	T-Note	T-Note +1.5	T-Note + 2.5	T-Note +2.5
7 Year Term	2 Yr Int Only	2 Yr Int Only	2 Yr Int Only	Level P&I
(10 Year amortization of principal and interest with balloon payment on remaining principal at the end of year 7)				
U.S. Loan Exposure Compared to Largest Eligible DE	70.7%	70.7%	84.9%	100.0%

Comments:

1. Installment payment program helps to mitigate the access to capital problem.
2. Steeper bid discount helps to mitigate cost of capital problem for very small business.
3. Increasing downpayment lowers risk to U.S. Government from financing smaller entities.
4. Immediate cash payment to U.S. Treasury is the same for all eligibles.
5. Amortize note on a ten year schedule, modified by interest only period, but principal balance due and payable after 7 years.

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WebCel Suggestions for Mitigating the Risk of the DE Program with Continuing Installment Payments

1. Enforce existing Rules - no restructuring or debt forgiveness.
2. Co-mingle DEs with non-DEs for future auctions (as with LMDS).
3. Raise downpayment for smaller DEs.
(Provided that access and cost of capital issues are correctly addressed).
4. Reduce term of loan to 7 Years (Amortization Schedule of 10).
5. Place a ceiling on the number of PoPs any DE can acquire (e.g., 25%).
6. FCC conducts due diligence on winning DEs prior to the granting of licenses to increase the likelihood of repayment.
(Similar to historical broadcast Rules which required a financial certification of ability to build and operate for some period of time.)
7. Bankruptcy law subordinated to the Commission's lien.